201 Mission Street, Suite 2400, San Francisco, CA 94105 T. 415.284.6999 F. 415.817.6945

November 18, 2004

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, DC 20551

Re: Regulation E-Docket No. R-1210

Dear Ms. Johnson:

The California Bankers Association appreciates this opportunity to submit this letter on the proposed changes to Regulation E. CBA is a professional nonprofit organization established in 1891 representing most of the depository financial institutions operating in California. CBA supports the Federal Reserve's efforts to improve the clarity of Regulation E as applied to emerging banking services. Generally, as discussed below, CBA favors a moderate regulatory approach to ensure that any regulation does not create unintended consequences.

Payroll cards

CBA recommends that payroll cards are not covered as regular deposit accounts under Regulation E, but rather in a manner similar to how electronic benefit transfers ("EBT") are treated under Section 202.15. Contrary to the Board's assertion, payroll card products are not offered as substitutes for traditional checking accounts. Payroll cards are used by employers as efficient means of administering payroll in lieu of issuing payroll checks. Employees gain access to funds typically through ATMs and point of sale facilities, and generally will have no rights to draw items against, or make deposits into, the employer-established account. As with EBT, the characteristics and limitations associated with the use of payroll cards justify different treatment under Regulation E. CBA would support, or example, applying the EBT alternative to periodic statements to payroll cards.

Unlike ongoing deposit accounts, funds accessible by payroll cards serve the limited purpose of disbursing employment compensation. The funds are more volatile, the transactions are fewer and concentrated at payroll dates (beginning and middle of month), there are no interest calculations, no traditional account fees, no traditional records of deposits and withdrawals, etc. In other words, very few of the reasons that justify the issuance of traditional monthly statements exist with respect to employees' use of payroll accounts. Moreover, producing statements and delivering them are very expensive, so this requirement would create a disincentive for banks to offer this type of service that would be economically attractive for employers.

The Board should also consider clarifications related to specific kinds of cards used in the employment context that are not used to disburse salary compensation. CBA recommends that

the Board state clearly that Regulation E will not apply, for example, to disbursements related to benefits that may be accessible by a card. For example, the Board should clarify that Health Savings Accounts are not covered, even though the account may permit card access, and an employer's funding of an HSA may be characterized as compensation.

Effect of definition of "account" on other laws and regulations. Proposed Section 205.2(b)(3) would provide that the term "account" includes an employer-established "payroll card account" used to pay a consumer's employment compensation on a recurring basis. A payroll card account would be subject to Regulation E whether the account is operated or managed by the employer, a third-party payroll processor, or a depository institution. CBA believes that, before adopting this change, the Board should first fully consider how the proposed definition would affect such accounts under other laws and regulations. A change in Regulation E to a fundamental term such as "account" could cause confusion, uncertainty, and unintended consequences.

For example, how are such cards to be treated for purposes of the reserve requirements under Regulation D? If reserves will be required, then offering and maintaining such accounts will be costly. Is the consumer in receipt of a payroll card a "customer," "consumer," or neither for purposes of Regulation P, the privacy regulations promulgated pursuant to the Gramm-Leach-Bliley Act, by virtue of using a payroll card "account"? For purposes of Regulation CC (Expedited Funds Availability Act), an "account" refers to the Regulation D definition of "deposit" that is a transaction account.[1] Would then a bank be required to furnish the funds availability disclosure before opening a payroll card account? Are the general disclosure requirements of Regulation DD (Truth in Savings Act) applicable to a payroll card account?[2] Finally, how payroll cards are treated federally may influence how states treat them for purposes of state escheat laws.

Before issuing a final rule, the Board should carefully consider the overall regulatory and market impact of the proposal and to work with the other federal banking agencies to identify common regulatory goals with respect to payroll cards and other forms of pre-paid and stored value cards. If the Board intends to treat payroll cards as accounts for purposes of Regulation E and other laws and regulations, then it should separately issue proposals for public comment to ensure that banks will have sufficient regulatory guidance.

We add that the applicability of these additional regulatory requirements will certainly increase the costs of providing payroll card products and similar products. The result would be that depository financial institutions would be discouraged from offering them, or such products will be unduly expensive. In the alternative, the Board should clarify in the staff commentary that the proposed Regulation E definition applies to that regulation only.

Financial institution. At pages 8-9 of the proposal, the Board suggests that a financial institution involved in offering a payroll card account may meet the definition of a "financial institution" under Regulation E. In the archetypical situation where an employer establishes an

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[1] Regulation D §§ 204.2(a)(1)(i) and 204.2(e), respectively.
[2] Regulation DD § 230.3.

account and deposits employee salary funds into it, the bank should not be deemed to be a financial institution within Regulation E. Although an employee will have access to the account through a card, the account is a business account not covered by Regulation E. The employer should be solely responsible for compliance with Regulation E. The consumer account exists only in the relationship between the employer and the employee.

NSF fee via EFT. New comment 3(b)-3 states that when an EFT is debited from a customer's account to cover an NSF fee, the transaction is covered by Regulation E, and a consumer authorization is needed. The Board should clarify that the consumer's authorization is required if the merchant or other payee initiates an EFT debit in order to recover the fee, but not if the paying bank assesses the fee. The bank's action is already disclosed in, and governed by, the applicable account agreement.

Transition period. In the event the Board determines that payroll card accounts are subject to Regulation E, CBA believes that a period of up to one year is an appropriate transition period.

Electronic Check Conversion

Signed authorizations. We note that the National Automated Clearing House Association ("NACHA") issues rules regarding consumer authorization for debits to consumer accounts. While a Regulation E requirement for signed authorizations for payees to convert checks received at POS locations would ensure customer consent and establish evidence of that consent, the Board should consider the burden this would place on retail establishments, and on the additional time required for each transaction. Permitting NACHA to develop the rules would foster more flexibility.

Coverage. The language in proposed § 205.3(b)(2)(i) is overly broad. It states that Regulation E "applies where a check, draft, or similar paper instrument is used as a source of information to initiate a one-time electronic fund transfer from a consumer's account." This language fails to limit the coverage to those instances where a consumer has provided a check solely for the purpose of initiating an EFT. This broad language may result in Regulation E coverage of transactions arising from the exchange of electronic check information or images through electronic information or image files, which also involves using a check as a "source of information." This clarification would help preserve a bright line between UCC coverage of, for example, electronic presentment, and Regulation E coverage.

Model disclosures—A(6). We note initially that a merchant in some cases may use several means of processing a payment. A merchant should be able to elect a payment mechanism that is economical, efficient, and prompt, and should not be required to detail such options in, or be limited by, the notice to the consumer. Therefore, any notice requirements should not impair a payee's ability to get paid.

The Board solicits comment on whether payees obtaining alternative authorizations should be required to specify the circumstances under which a check that can be used to initiate an EFT will be processed as a check. Such a disclosure would be too complex, and it may not be practical to list all the circumstances where a transaction may be processed by check. A payee

may intend to process a check as an EFT, but then is unable to do so or finds a more efficient way to process the transaction. Merchants and their banks need the flexibility to process an authorized transaction and to obtain payment. Moreover, listing all the reasons could confuse consumers rather than help them.

Comment 3(b)(2)-2. This proposed comment states that if a payee obtains a consumer's authorization to use a check solely as a source document to initiate an EFT, the payee cannot process the transaction as a check. This is too restrictive because in some instances, an ECK transaction may be rejected by the paying bank and the payee may be required to use the original check to complete the transaction. Use of model clause A-6(c) might not help because of the risk is that the payee did not list all specific circumstances under which the payment could be processed as a check. For the reasons stated above, CBA believes some allowance must be made for the payee to process as a check, and that model clause A-6(c) should be eliminated.

Notice of error from consumer. With regard to proposed commentary 11(b)-7, the meaning of the following is unclear: "Where the consumer's assertion of error involves an unauthorized EFT, however, the institution must comply with § 205.6 before it may impose any liability on the consumer." Please clarify the portion of § 205.6 that applies.

Time limits and extent of investigation. It would be burdensome for a bank to review "all information" within its records in the course of investigating a claim. If the claim involves an allegedly unauthorized ACH transaction, a bank would not be permitted to limit its investigation to the payment instructions where additional information within its own records could be dispositive of the consumer's claim, as is currently permitted. Such a review could be highly burdensome because records could be located in different locations. This comment should not be adopted.

ATM Disclosures

CBA strongly supports the Federal Reserve's proposal to amend the Official Staff Interpretations to Regulation E regarding ATM notices. The preamble to the proposal accurately describes the need to permit banks to provide accurate notices. Many ATM operators charge some ATM users a fee but not others, so the existing guidance, if followed strictly, would be misleading to consumers.

Major segments of the industry have provided disclosure since October, 2001 that is accurate and fully protective of consumers. Such disclosure alerts consumers through signage that a fee "may" be imposed, followed by a precise, individualized disclosure on the screen that sets forth, if a fee in fact will be imposed, that fact and the amount of the fee. That disclosure pattern is being attacked in a major law suit that thus far involves as defendants five of this country's larger financial institution ATM operators. It is important that the Board provide clarification with respect to this ATM signage requirement.

Permitting ATM operators who do not universally charge consumers for EFT services to use language indicating that a fee may be imposed is consistent with EFTA § 904(d)(3)(A) and will serve to alert consumers to the more consumer-specific on-screen disclosures provided after card

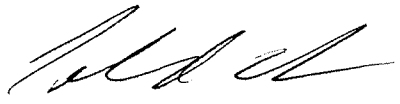
insertion. The more detailed on-screen notice, which will use the explicit language of Regulation E to notify consumers of the precise fee amount, if any, will ensure that a consumer receives adequate disclosure before he or she proceeds with an ATM transaction.

Further, we urge the Board to make clear in the supplemental information accompanying the final rule that the proposed revisions merely clarify the current ATM fee disclosure requirements. The failure to make such a clarification could lead to the misinterpretation that the revisions are only prospective in nature and do not reflect the current state of the rule.

Limitations. Regulation E does not contain a time limitation that would preclude a consumer from asserting a claim of an unauthorized EFT, even though EFTA § 915(g) establishes a one-year statute of limitations. Therefore, CBA recommends for purposes of clarity that Regulation E incorporate this limitation period. This addition would be consistent with the expedited recredit provisions of the Check Clearing for the 21st Century Act ("Check 21") and Regulation CC § 229.56(c), which are modeled after the error resolution structure of Regulation E.

CBA appreciates this opportunity to submit these comments on behalf of its members. If you have any questions or comments, please do not hesitate to contact me.

Sincerely,



Leland Chan
General Counsel